

must keep copies in your files of the NASDAQ listings (or the Wall Street Journal) or written quotations from the market makers quoting the Publicly Traded and Marketable securities which support the adjustment.

(5) If your net unrealized gains on Publicly Traded and Marketable securities are more than 30 percent below their original level on the first business day of any calendar quarter, and remain so for the next 30 days, you agree to do one of the following to remain in compliance with the terms of your Leverage:

(i) By the first day of the next calendar quarter, increase your Regulatory Capital sufficiently to restore support for the increased limit; or

(ii) Lower the increased limit to reflect the decrease in net unrealized gains on Publicly Traded and Marketable securities, and reduce any Financings that exceed the lower limit.

*Example to paragraph (c) of this section.* Your Regulatory Capital is \$2,500,000 and your overline limit is \$500,000 (20 percent of \$2,500,000). On January 15, 1995, you document net unrealized gains on Publicly Traded and Marketable securities of \$200,000 and compute an increased limit of \$540,000 (20 percent of \$2,700,000). You now make an investment of \$540,000 in a Small Business. Nothing changes until the first business day of April, 1996, when you document net unrealized gains on Publicly Traded and Marketable securities of only \$120,000, a reduction of more than 30 percent. Your net unrealized gains remain at this level for the next 30 days. Your increased limit is now only \$524,000 (20 percent of \$2,620,000). By July 1, 1996, you must either increase Regulatory Capital by \$80,000 to restore your increased limit to \$540,000, or reduce your portfolio investment from \$540,000 to \$524,000.

[61 FR 3189, Jan. 31, 1996, as amended at 63 FR 5867, Feb. 5, 1998; 64 FR 70996, Dec. 20, 1999]

**§ 107.750 Conditions for financing a change of ownership of a Small Business.**

You may finance a change of ownership of a Small Business only under the conditions set forth in this section.

(a) The Financing must:

(1) Promote the sound development or preserve the existence of the Small Business;

(2) Help create a Small Business as a result of a corporate divestiture; or

(3) Facilitate ownership in a Disadvantaged Business.

(b) The Resulting Concern (as defined in paragraph (c) of this section) must:

(1) Be a Small Business under § 107.700;

(2) Have 500 or fewer full-time equivalent employees; or meet one of the appropriate debt/equity ratio tests:

(i) If you have outstanding Leverage, the Resulting Concern's ratio of debt to equity must be no more than 5 to 1; or

(ii) If you have no outstanding Leverage, the Resulting Concern's ratio of debt to equity must be no more than 8 to 1.

(c) *Definitions.* (1) The "Resulting Concern" is determined by viewing the business as though the change of ownership had already occurred, giving effect to all contemplated financing, mergers, and acquisitions.

(2) For purposes of this section, "debt" means long-term debt, including contingent liabilities, but excluding accounts payable, operating leases, letters of credit, subordinated notes payable to the seller, any other liabilities approved for exclusion by SBA and short-term working capital loans (so long as the loans carry a zero balance for 30 consecutive days during the concern's fiscal year).

(3) For purposes of this section, "equity" means common and preferred stock (corporation), contributed capital (partnership), or membership interests (limited liability company).

**§ 107.760 How a change in size or activity of a Portfolio Concern affects the Licensee and the Portfolio Concern.**

(a) *Effect on Licensee of a change in size of a Portfolio Concern.* If a Portfolio Concern no longer qualifies as a Small Business you may keep your investment in the concern and:

(1) Subject to the overline limitations of § 107.740, you may provide additional Financing to the concern up to the time it makes a public offering of its securities.

(2) Even after the concern makes a public offering, you may exercise any stock options, warrants, or other rights to purchase Equity Securities which you acquired before the public offering,

or fund Commitments you made before the public offering.

(b) *Effect of a change in business activity occurring within one year of Licensee's initial Financing*—(1) *Retention of Investment*. Unless you receive SBA's written approval, you may not keep your investment in a Portfolio Concern, small or otherwise, which becomes ineligible by reason of a change in its business activity within one year of your initial investment.

(2) *Request for SBA's approval to retain investment*. If you request that SBA approve the retention of your investment, your request must include sufficient evidence to demonstrate that the change in business activity was caused by an unforeseen change in circumstances and was not contemplated at the time the Financing was made.

(3) *Additional Financing*. If SBA approves your request to retain an investment under paragraph (b)(2) of this section, you may provide additional Financing to the Portfolio Concern to the extent necessary to protect against the loss of the amount of your original investment, subject to the overline limitations of § 107.740.

(c) *Effect of a change in business activity occurring more than one year after the initial Financing*. If a Portfolio Concern becomes ineligible because of a change in business activity more than one year after your initial Financing you may:

- (1) Retain your investment; and
- (2) Provide additional Financing to the Portfolio Concern to the extent necessary to protect against the loss of the amount of your original investment, subject to the overline limitations of § 107.740.

#### STRUCTURING LICENSEE'S FINANCING OF ELIGIBLE SMALL BUSINESSES: TYPES OF FINANCING

##### **§ 107.800 Financings in the form of Equity Securities.**

(a) You may purchase the Equity Securities of a Small Business. You may not, inadvertently or otherwise:

- (1) Become a general partner in any unincorporated business; or
- (2) Become jointly or severally liable for any obligations of an unincorporated business.

(b) *Definition*. Equity Securities means stock of any class in a corporation, stock options, warrants, limited partnership interests in a limited partnership, membership interests in a limited liability company, or joint venture interests. If the Financing agreement contains debt-type acceleration provisions or includes redemption provisions other than those permitted under § 107.850, the security will be considered a Debt Security for purposes of § 107.855.

##### **§ 107.810 Financings in the form of Loans.**

You may make Loans to Small Businesses. A Loan means a transaction evidenced by a debt instrument with no provision for you to acquire Equity Securities.

##### **§ 107.815 Financings in the form of Debt Securities.**

You may purchase Debt Securities from Small Businesses.

(a) *Definitions*. Debt Securities are instruments evidencing a loan with an option or any other right to acquire Equity Securities in a Small Business or its Affiliates, or a loan which by its terms is convertible into an equity position, or a loan with a right to receive royalties that are excluded from the Cost of Money pursuant to § 107.855(g)(12). Consideration must be paid for all options that you acquire.

(b) *Restriction on options obtained by Licensee's management and employees*. If you have outstanding Leverage or plan to obtain Leverage, your employees, officers, directors or general partners, or the general partners of the management company that is providing services to you or to your general partner, may obtain options in a Financed Small Business only if:

- (1) They participate in the Financing on a *pari passu* basis with you; or
- (2) SBA gives its prior written approval; or
- (3) The options received are compensation for service as a member of the board of directors of the Small Business, and such compensation does not exceed that paid to other outside directors. In the absence of such directors, fees must be reasonable when